Office of Chief Counsel
Internal Revenue Service

memorandum

CC:SB/SE:DEN:2:TL-N-3434-01
RDD'Estrada

date: September 17, 2001

to: Governmental Liaison, C&L, Area 6
Attn: Barbara Haugh

from: Associate Area Counsel, Denver

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subject: **Validity of Tax Return and Statute of Limitations**
Taxpayer: [redacted]

This responds to your request for advice on whether the [redacted] federal form 1040 of the above-referenced taxpayer constitutes a valid return and, if so, whether a failure to report the amount of recapture on a sale constitutes an omission for purposes of the statute of limitations.

ISSUE

1. Whether a document filed on the proper form and purporting to be a [redacted] income tax return which contains a seemingly valid computation of tax liability, but which changes the jurat and attaches a written request for a determination of status for tax purposes and an affidavit which questions the application of the tax laws to [redacted] is a valid tax return.

2. Whether the failure to report recapture under I.R.C. § 1245 where the underlying asset sold is reported, constitutes an omission for purposes of the six year statute of limitations provided for in I.R.C. § 6501(e).

CONCLUSION

1. The [redacted] document is a valid federal income tax return as it satisfies all of the elements of a return.

2. The failure to report recapture under I.R.C. § 1245 constitutes an omission for purposes of the statute of limitations under I.R.C. § 6501(e) where, although the sale of the underlying asset is reported by the Subchapter S corporation, there is nothing on the shareholder's return to indicate that

capital gain reported is attributable to the sale by the corporation.

FACTS

On [redacted], [redacted] delivered his [redacted] Form 1040 to Special Agent Wanda Dietz. The return was not signed but accompanying the return was a cover letter which declared under penalties of perjury that all financial information was true and correct. Also attached to the return were two documents [redacted] indicated he previously had sent to the Internal Revenue Service: "Written Request for Verified Determination of Status for Tax Purposes Letter, Prior to Filing of Tax Returns;" and "Contract and Declaration of Citizenship." [redacted] indicated these documents were originally mailed to the Internal Revenue Service on [redacted].

[redacted] indicated to the special agent his belief that he was not required to file a return because he is a nonresident but on more than one occasion admitted that he could be wrong on his position.

The [redacted] Form 1040 reports distributions from three Subchapter S corporations; [redacted], [redacted] and [redacted]. Also reported is capital gain from an installment sale on a Form 6252 apparently from a sale by [redacted] who reported a sale but not recapture under I.R.C. § 1245 on the property sold.

ANALYSIS

1. Validity of Return

The following four-part test determines whether a document is a valid federal income tax return: "First, there must be sufficient data to calculate tax liability; second, the document must purport to be a return; third, there must be an honest and reasonable attempt to satisfy the requirements of the tax law; and fourth, the taxpayer must execute the return under penalties of perjury." Beard v. Commissioner, 82 T.C. 766, 777 (1984), aff'd per curiam, 793 F.2d 139 (6th Cir. 1986).

The document in the present case is on a Form 1040 and has a preparer's stamp although no preparer's signature. On its face, the document contains sufficient data to calculate tax liability

and it purports to be a return. It appears the only missing elements of a valid return is a signature on the return "under penalties of perjury" and a clear indication that the document purports to be a return.

Attached to the return is a cover letter dated [redacted] which states in part that

> . . . I certify that these are true and correct returns to the best of my knowledge and fairly represent the financial activities during [redacted]. Furthermore, I declare under penalty of perjury under the laws of the united states of America that all financial information, to the best of my knowledge, is true and correct. . . .

Although this declaration is not the exact language of the Form 1040 jurat[1], in our opinion it is a sufficient declaration that the Form 1040 is made under the penalties of perjury in accordance with I.R.C. § 6065. See, Williams v. Commissioner, 114 T.C. 136 (2000) and cases cited therein. This is unlike the situations where taxpayers add a disclaimer to the preprinted jurat, Sloan v. Commissioner, 102 T.C. 137 (1994), aff'd, 53 F.3d 799 (7th Cir. 1995), Williams v. Commissioner, supra; strike through the preprinted jurat, Borgeson v. United States, 757 F.2d 1071 (10th Cir. 1985), Hettig v. U.S., 845 F.2d 794 (8th Cir. 1988), Mosher v. Internal Revenue Service, 775 F.2d at 1292 (5th Cir. 1985); substitute language which states the information is estimated, Jenkins v. Commissioner, T.C. Memo. 1989-617; or fail to file returns because of a belief the jurat is an oath which their religion forbids, U.S. v. Dawes, 874 F.2d 746 (10th Cir. 1989).

The Written Request for Verified Determination of Status for Tax Purposes Letter, Prior to Filing of Tax Returns" and "Contract and Declaration of Citizenship" do not impugn [redacted]'s declaration contained in the cover letter but are in support of his belief he is not required to file a tax return. The filing of the return, together with his repeated statements that although he is of the belief he is not required to file because

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[1] The Form 1040 jurat provides as follows: "Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge."

of his nonresident status he may be incorrect in his position, evidence an intent to file a tax return.

Although it is a close call, we are of the opinion that the [redacted] Form 1040 submitted to Special Agent Wanda Dietz, taken together with his cover letter and statements made at the time the document was submitted, constitute a valid income tax return and should be processed as such.[2]

We are also aware that [redacted] is under criminal investigation for [redacted]. Accordingly, no civil action should proceed on the [redacted] taxable year without first coordinating and receiving the approval of the criminal investigation division.

2. Statute of Limitations

Normally, the statute of limitations on assessment is three years from the filing of a return. I.R.C. § 6501(a). However, I.R.C. § 6501(e) provides that if a taxpayer omits from a return more than 25% of the amount of gross income stated in the return a six year statute of limitations on assessment applies. For purposes of this section gross income from a trade or business, including a partnership or Subchapter S corporation, means the taxpayer's percentage of the gross receipts of the trade or business. I.R.C. § 6501(e)(A)(i). See Insulglass Corp. v. Commissioner, 84 T.C. 203 (1985); Estate of Klein v. Commissioner, 63 T.C. 585 (1975), aff'd 537 F.2d 701 (2nd Cir. 1976); Connelly v. Commissioner, T.C. Memo. 1982-644.

In the present case, the sale of assets by [redacted] was a sale not in the ordinary course of business, i.e., the corporation was not in the business of selling equipment. Therefore, [redacted] cannot be credited with the gross receipts of the corporation on the sale of this equipment. See The Colony, Inc. v. Commissioner, 357 U.S. 28 (1958).

The omitted item on [redacted]'s [redacted] return is the failure to report recapture under I.R.C. § 1245 from [redacted]

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[2] In connection with the criminal investigation of the taxpayer for the taxable year [redacted] for willful failure to file a return in violation of I.R.C. § 7203, we opined that this document constituted a valid income tax return and that a successful criminal prosecution under section 7203 would be unlikely.

a Subchapter S corporation, in connection with the sale of assets of that corporation. ICP reported the sale but did not report recapture under I.R.C. § 1245 on the property sold. We understand that the recapture income is approximately $[redacted] and if taken into consideration is sufficient to constitute an omission of gross income in excess of [redacted]%. Such recapture on the entire sale is required to be reported in the year of sale notwithstanding application of the installment sales provisions. I.R.C. § 453(i). [redacted] reported a capital gain on Schedule D from an installment sale reported on Form 6252 but there is no indication that this sale was the sale of assets by the Subchapter S corporation.

I.R.C. § 6501(e)(A)(ii) provides that "in determining the amount omitted from gross income, there shall not be taken into account any amount which is omitted from gross income stated in the return if such amount is disclosed in the return, or in a statement attached to the return, in a manner adequate to apprise the Secretary of the nature and amount of such item."

Because the recapture amount would have been difficult, if not impossible, to determine from [redacted]'s returns and the supplemental information attached to them, it is reasonable to take the position that [redacted] did not disclose the amount of recapture in the return or a statement attached to the return in a manner adequate to apprise the Secretary of the nature and amount of such item. Therefore, the exception to the six year statute of limitations on assessment under section 6501(e)(A)(ii) does not apply and the Service has six years to assess from the date the return was filed.

In an abundance of caution, we suggest that you contact the criminal investigation division and seek permission to obtain a consent from [redacted] to extend the period for assessment on the [redacted] return.

Should you have any questions, please contact the undersigned at (303) 844-2214, Ext. 271.

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APPROVED:

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